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ABSTRACT

More than $25 billion in financial aid in 1988 is awarded annually to students attending postsecondary education. The aid covers about the same percentage of college costs that it did in 1970, but the impact of veterans' education benefits and social security benefits is no longer significant, and loans now make up one-half the total aid, having supplanted grants as the basic form of support for students who can demonstrate need. Participation rates in postsecondary education have not increased appreciably since the mid-1970s. Some ways of increasing participation, particularly of low income and minority students, are to increase funding for grants, decrease loan defaults by increasing risk sharing, and simplify the aid application process. To increase the participation of older students, the tax exemption for all employer-paid postsecondary expenses should be restored and a partnership should be formed between the public and the private sectors to provide adequate financial aid to dislocated workers. Economically disadvantaged students who want to attend college must compete for the same aid with other economically disadvantaged students who want to attend vocational schools. Those funds should be better targeted by setting different award and loan schedules for students in collegiate and vocational programs; limiting the eligibility of students who do not have a high school diploma or equivalent; and removing students without a high school degree from the postsecondary student aid programs and placing them in vocational training programs of the Departments of Education and Labor. Changes should be made in calculating family income to offset "middle class creep" in programs originally intended to help economically disadvantaged students. (10 references) (CML)

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# 13. ISSUES IN FINANCING POST-SECONDARY EDUCATION AND TRAINING

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## Introduction

More than $25 billion in financial aid is awarded annually to students attending post-secondary education. This aid is provided in a variety of forms, including grants and fellowships, loans, and service-related aid, and comes from many sources -- the federal and state governments, the educational institutions themselves, employers, and the philanthropic sector.

This paper describes how post-secondary education and training is currently financed in this country, discusses whether the aid system operates in an effective and productive manner, and suggests ways in which it might be improved. The first section of the paper examines the amount of aid that is available to individuals enrolling in post-secondary education and training programs, the proportion of students' costs of attendance that is covered by this assistance, and the distribution of aid according to student and institutional characteristics. The second section identifies a number of concerns relating to the ineffectiveness of the current system in meeting the goal of equal educational opportunity. Special emphasis in this paper is given to the situation of students enrolled in vocational programs, in community colleges, and in the proprietary sector. These students

make up a growing share of post-secondary enrollments and have consumed proportionately greater shares of student assistance funds in the past decade. The conflicting goals and needs of vocational students versus a system of student assistance designed to benefit students pursuing traditional higher education are examined throughout this paper.[1]

## I. The Current System of Student Financial Aid

### Trends in Aid Availability

Student financial assistance has played an important role in the financing of post-secondary education since the GI Bill was passed following the Second World War. Through the GI Bill, millions of returning veterans from three separate wars have been afforded the opportunity to pay for a college education in return for the service they provided to their country. The National Defense Education Act (NDEA) in 1958 shifted the federal emphasis of "aid for service" to one of providing incentives for students to enroll in certain types of educational programs, particularly in the sciences and engineering.

In the 1960s another shift in the philosophy of providing federal student assistance occurred. The passage of the Higher Education Act in 1965 was motivated by a growing national sentiment to increase opportunities for economically and socially disadvantaged citizens. The federal commitment to equal educational opportunity was established through this legislation, and was strengthened by the 1972 Education Amendments with the creation of Basic Educational Opportunity Grants (since renamed Pell Grants). Pell Grants were designed to serve as a "floor" of support for the neediest students, and are presently part of

a package of federal aid programs that includes grants, work-study, and student loans.

Since the early 1970s, federal aid has accounted for approximately three-quarters or more of all financial assistance awarded to students in post-secondary education. State level grant and loan programs presently provide an estimated $2 billion in assistance, or slightly less than 10 percent of aid from all sources. Institutionally awarded aid has been the largest growing component of student aid in the 1980s; in 1988, nearly $5 billion, or about 20 percent of aid from all sources, was provided through the institutions themselves. Other sources, including employer-paid education benefits and private and philanthropic aid, also help to fund some portion of educational expenses.

Chart 1 shows total dollar amounts awarded to post-secondary students since 1970 according to the major sources of support: federal government, state governments, and educational institutions. As the chart indicates, total student aid has grown from around $5 billion in the early 1970s to over $25 billion in 1988. In real terms, aid grew substantially in the early 1970s, levelled off somewhat in the latter part of the decade, and peaked in 1980. (See Table 1.) With the exception of the recent years, total aid in inflation adjusted terms throughout the 1980s has been lower than the 1980 peak.[2] Most of the real decline in aid during the 1980s has been the result of federal actions, while state and institutional aid has increased consistently, helping to temper decreases in federal support.[3]

Changes over time in categories of student aid are helpful in describing general trends in post-secondary financing since 1970.[4] As

CHART 1
AID AWARDED TO POST-SECONDARY STUDENTS,
BY SOURCE, 1970 TO 1988

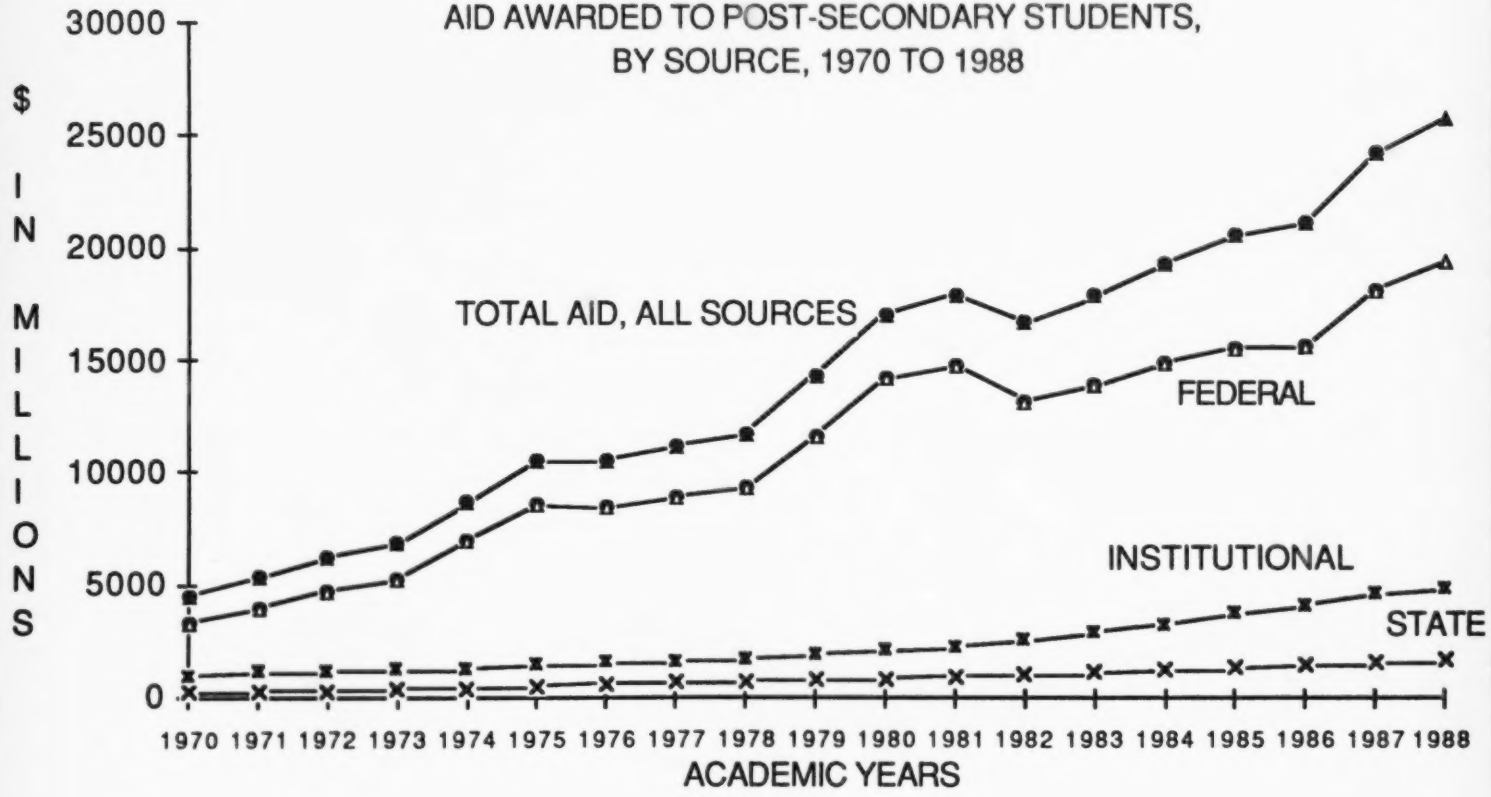


**Table 1**
**AID AWARDED TO POST-SECONDARY STUDENTS, BY CATEGORY OF AID AND MAJOR AID PROGRAMS, 1970 TO 1988**

| | Current Dollars, in Millions | | | | | Percent Change |
|---|---|---|---|---|---|---|
| | 1970 | 1975 | 1980 | 1985 | 1988* | 1970-88 |
| **Grants and Fellowships** | 1351 | 3146 | 5814 | 9106 | 11383 | 743% |
| Pell Grants | 0 | 937 | 2387 | 3567 | 4404 | na |
| State Grants | 236 | 490 | 801 | 1311 | 1642 | 596% |
| Institutional Aid | 965 | 1435 | 2060 | 3674 | 4793 | 397% |
| **Service-Related Aid** | 1847 | 5607 | 4460 | 1851 | 1791 | -3% |
| Social Security | 499 | 1093 | 1883 | 0 | 0 | -100% |
| Veterans Benefits | 1121 | 4180 | 1714 | 849 | 740 | -34% |
| College Work Study | 227 | 295 | 660 | 656 | 692 | 205% |
| **Student Loans** | 1298 | 1772 | 6959 | 9914 | 12986 | 900% |
| Stafford | 1015 | 1267 | 6203 | 8839 | 11812 | 1064% |
| Perkins | 241 | 460 | 694 | 703 | 874 | 263% |
| **TOTAL AID, ALL SOURCES** | 4496 | 10525 | 17233 | 20871 | 26160 | 482% |
| | Constant 1988 Dollars, in Millions | | | | | |
| **Grants and Fellowships** | 4117 | 6917 | 8349 | 10016 | 11383 | 176% |
| Pell Grants | 0 | 2060 | 3428 | 3923 | 4404 | na |
| State Grants | 719 | 1077 | 1150 | 1442 | 1642 | 128% |
| Institutional Aid | 2941 | 3155 | 2958 | 4041 | 4793 | 63% |
| **Service-Related Aid** | 5628 | 12327 | 6404 | 2036 | 1791 | -68% |
| Social Security | 1521 | 2403 | 2704 | 0 | 0 | -100% |
| Veterans Benefits | 3416 | 9190 | 2461 | 934 | 740 | -78% |
| College Work Study | 692 | 649 | 948 | 722 | 692 | 0% |
| **Student Loans** | 3955 | 3896 | 9993 | 10905 | 12986 | 228% |
| Stafford | 3093 | 2786 | 8907 | 9722 | 11812 | 282% |
| Perkins | 734 | 1011 | 997 | 773 | 874 | 19% |
| **TOTAL AID, ALL SOURCES** | 13701 | 23139 | 24746 | 22957 | 26160 | 91% |

* estimated

SOURCE: Lewis, 1988.

Table 1 shows grants and fellowships doubled in the 1970s in real terms and increased more than one-third in the 1980s. This growth was due largely to the establishment of the Pell Grants program, which now awards over $4 billion annually. State grant programs and institutional scholarships have also registered healthy increases in this time period, even when inflation has been taken into account.

Service-related aid, which accounted for more than one third of all aid awarded in 1970, has been reduced sharply in the past decade. Social Security education benefits, which totalled five to ten percent of all aid awarded throughout the 1970s, have now been completely phased out. At the same time, Veterans education benefits declined by three quarters, in real terms, since their use peaked in the mid-1970s. This has led to an overall reduction in service-related aid of two thirds in real dollars since 1970.

Student loans have registered large increases since the late 1970s, when eligibility for the Guaranteed Student Loan (GSL) (now Stafford) program was expanded. While loans accounted for approximately 10 percent of total aid provided in the early and mid-1970s, they now make up more than 50 percent of this total. The Stafford program alone grew nearly threefold in real dollars between 1970 and 1988. Student loans have clearly become a crucial element in the post-secondary education financing equation.

Chart 2 illustrates this point by showing the percentage of college costs of attendance that are met by the three categories of student aid. As the chart indicates, student aid as a proportion of costs grew substantially in the early 1970s, aided largely by increases

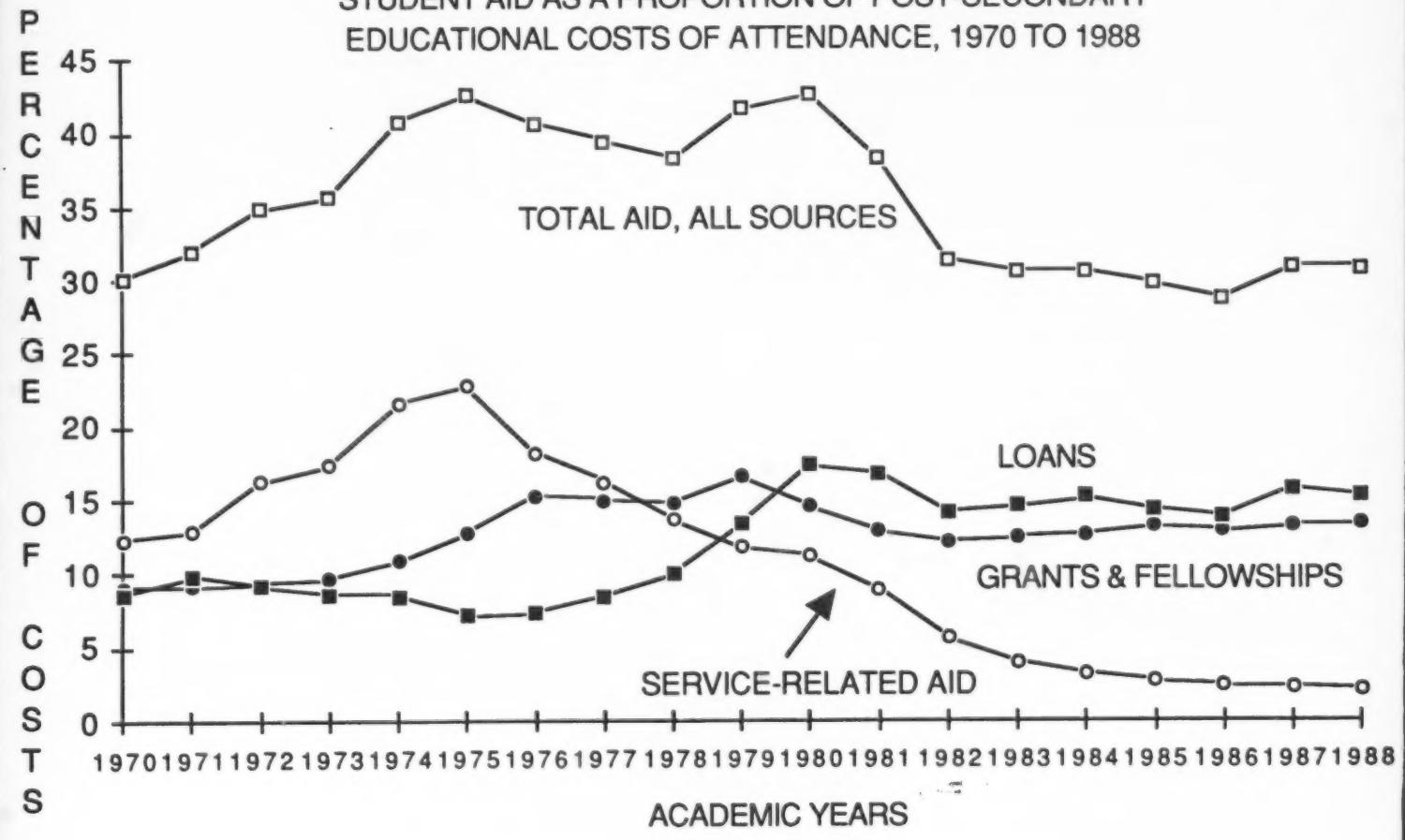
in aid awarded through the service-related programs and, to a lesser extent, through the growth in grants and fellowships. Since 1975, however, two very different trends have shaped the capacity of student aid to meet college costs. One is the dramatic decline in service-related aid, which met more than 20 percent of cost of attendance in 1975 but now covers barely two percent of total costs of attendance. The other is the steady increase in the reliance on loans as a means of paying for college; the proportion of costs met through loans in 1988 was nearly twice what it was in the mid-1970s.

Overall, student aid in 1988 covered roughly the same percentage of costs of attendance as it did in 1970. Total aid accounted for approximately 30 percent of college costs in 1970, rose to more than 40 percent in 1975 and, after a slight decline in the late 1970s, returned to this plus-40 percent level in 1980. Between 1980 and 1982, student aid fell from 43 percent of costs to 32 percent as a result of the initial round of Reagan administration budget cuts. Since then, student aid has hovered around 30 percent of attendance costs.

Trends in student aid availability thus have changed in several important ways since 1970. First, the sources and types of aid available have shifted significantly. While Veterans Education and Social Security benefits were an important source of aid through much of the 1970s, their relative impact on education financing has diminished to negligible levels in the late 1980s. Aid in return for service has been replaced by need-based grants and loans as the most important source of student assistance nationally. Second, loans have grown tremendously, especially since the late 1970s, and now form an integral

CHART 2

STUDENT AID AS A PROPORTION OF POST-SECONDARY EDUCATIONAL COSTS OF ATTENDANCE, 1970 TO 1988



part of the financing equation. With loans now making up one half of total aid, they appear to have supplanted grants as the basic form of support for students who can demonstrate need. Finally, while the mix of aid has changed since 1970, it presently does no more overall to help pay for college than it did in 1970.

## Who Receives Student Aid?

The distribution of student aid tells a great deal about how post-secondary education and training is being financed in the United States, and whether the aid is reaching its intended beneficiaries. Two types of distribution are discussed here: first, how aid is apportioned to students by the sector of institution attended and, second, what are the characteristics of students who receive aid.

Regrettably, data on student aid recipients has neither been consistently nor completely collected over time. While time series data for some programs are adequate, in many cases the quality of the information is poor or nonexistent. For the purposes of this paper we focus on general demographic data for specific programs and then attempt to generalize about broader trends from this information. Data from a 1986 comprehensive study of post-secondary educational financing, the National Postsecondary Student Aid Study (NPSAS), is also included in order to give some sense of overall financing as it exists today.

## Aid By Type of Institution

Table 2 shows the distribution of aid by sector for several federal aid programs. The table indicates trends since 1973 -- the

first year of operation for the Pell Grants program -- for both Pell and the so called campus-based programs of Perkins Loans, College Work Study, and Supplemental Educational Opportunity Grants.[5] As indicated, the share of Pell dollars going to students in public two year institutions steadily declined through the middle and late 1970s; from a peak of 27 percent in 1974, the proportion has levelled off at just under 19 percent throughout the 1980s. At the same time the proportion of aid awarded to students in public four year schools, as well as private institutions, has also declined, particularly since 1980.

The decline in the share of Pell Grant dollars going to students in the collegiate sector has occurred because of the rapid growth in the amount of Pell aid that goes to proprietary school students. The share of Pell Grant dollars going to proprietary school students has grown from a low of 7 percent in the initial year of 1973 to the point where students in this sector now receive one quarter of all Pell monies awarded annually. Indeed, by 1985 proprietary students actually received more Pell assistance than students in all private, non-profit institutions of higher education.

Similar trends have taken place with the campus-based programs, though on a lesser scale. Students in community colleges received slightly less of all campus-based funding in 1987 (10 percent) than they did in 1973 (12 percent). The proportion of total campus-based funding going to public four year students dropped from 49 percent to approximately 42 percent in the mid-1980s. By contrast, campus-based aid going to students in private institutions increased from 36 to 38 percent in the middle 1970s to about 42 or 43 percent in the middle

Table 2
PERCENTAGE DISTRIBUTION OF AID, BY INSTITUTIONAL TYPE, FOR THE PELL AND CAMPUS-BASED PROGRAMS, 1973 TO 1987

Pell Grants Program

| | Public 2-Yr | Public 4-Yr | Private | Proprietary | Total |
|---|---|---|---|---|---|
| 1973 | 24.9% | 41.2% | 26.3% | 7.6% | 100.0% |
| 1974 | 26.7% | 40.1% | 24.4% | 8.8% | 100.0% |
| 1975 | 26.1% | 39.0% | 24.8% | 10.1% | 100.0% |
| 1976 | 23.4% | 42.8% | 24.6% | 9.2% | 100.0% |
| 1977 | 24.3% | 42.8% | 23.3% | 9.7% | 100.0% |
| 1978 | 23.2% | 39.4% | 26.8% | 10.6% | 100.0% |
| 1979 | 21.8% | 39.6% | 28.1% | 10.5% | 100.0% |
| 1980 | 18.6% | 41.1% | 28.8% | 11.5% | 100.0% |
| 1981 | 18.7% | 40.7% | 27.1% | 13.5% | 100.0% |
| 1982 | 18.2% | 38.7% | 26.6% | 16.6% | 100.0% |
| 1983 | 18.5% | 38.0% | 24.6% | 18.8% | 100.0% |
| 1984 | 18.4% | 37.7% | 23.0% | 20.8% | 100.0% |
| 1985 | 18.8% | 37.0% | 21.9% | 22.1% | 100.0% |
| 1986 | 18.7% | 35.7% | 20.8% | 24.8% | 100.0% |
| 1987* | 18.7% | 35.5% | 20.1% | 25.7% | 100.0% |

Campus-Based Programs

| | Public 2-Yr | Public 4-Yr | Private | Proprietary | Total |
|---|---|---|---|---|---|
| 1973 | 11.9% | 49.0% | 38.1% | 1.1% | 100.0% |
| 1974 | 12.7% | 47.6% | 36.8% | 2.9% | 100.0% |
| 1975 | 11.8% | 46.9% | 37.2% | 4.1% | 100.0% |
| 1976 | 11.8% | 47.2% | 36.0% | 4.9% | 100.0% |
| 1977 | 11.5% | 47.0% | 35.8% | 5.7% | 100.0% |
| 1978 | 11.0% | 44.8% | 37.4% | 6.9% | 100.0% |
| 1979 | 10.4% | 43.4% | 40.9% | 5.3% | 100.0% |
| 1980 | 10.1% | 43.0% | 41.8% | 5.2% | 100.0% |
| 1981 | 10.3% | 42.5% | 42.0% | 5.1% | 100.0% |
| 1982 | 9.8% | 43.3% | 42.0% | 4.9% | 100.0% |
| 1983 | 9.7% | 42.8% | 42.5% | 5.1% | 100.0% |
| 1984 | 9.6% | 42.7% | 42.7% | 4.9% | 100.0% |
| 1985 | 9.8% | 41.6% | 43.3% | 5.3% | 100.0% |
| 1986 | 9.7% | 41.8% | 42.9% | 5.6% | 100.0% |
| 1987* | 9.6% | 42.1% | 43.0% | 5.3% | 100.0% |

* Estimates, U.S. Department of Education

SOURCE: U.S. Department of Education, 1987; Lewis, 1988.

1980s. Proprietary school students, while continuing to receive the smallest share of campus-based aid of any sector, did have the largest relative increase, from 1 percent in 1973 to slightly more than 5 percent in the mid-1980s.

Comparable data on the distribution of aid over time for other programs, by sector, is inadequate or unavailable. However, the evidence available would suggest that the proportion of aid going to proprietary school students is increasing in many other programs as well. For example, unofficial estimates of the percentage of Stafford loan dollars going to students in proprietary schools show an increase from approximately 15 percent of all loans in 1979 to nearly 35 percent in 1987.[6]

When the aid received by community college students enrolled in vocational programs is combined with the aid received by proprietary school students, we estimate that the percentage of all aid currently awarded to vocational students is approximately 30 percent.[7] This percentage varies by program, however, and has changed measurably in the past decade. For example, the percentage of Pell Grant dollars awarded to vocational students rose from approximately 15 percent in the mid 1970s to nearly 35 percent in the mid-1980s. While no time series data on the distribution of loans are available, information from selected state agencies indicates that the proportion of loans borrowed by proprietary school students has substantially increased. Thus unofficial estimates indicate that approximately 40 percent of Stafford loans and more than 60 percent of Supplemental Loans for Students loans currently are provided to vocational students. For the federal campus-

based programs, a slight decline in aid awarded to community college students roughly offsets gains for the proprietary sector, resulting in a stable 10 percent share for vocational students over the past decade. For other programs, the proportion of aid received by vocational students is 10 percent or less, with the exception of the GI Bill where we estimate that 20 percent of aid goes to students in vocational programs.

The 1986 NPSAS survey provides information on the proportion of students who receive federal aid. According to the survey, of all undergraduates enrolled in post-secondary education programs in the fall of that year, slightly over one third -- 35 percent -- received some form of federal student aid. By sector, 29 percent of all students in public institutions received federal aid, compared to 48 percent of students in private colleges, and an astounding 81 percent of students in proprietary institutions (Center for Education Statistics, 1988). This data suggests that students in vocational programs are much more likely to receive federal aid than are students in academic programs.

### The Characteristics of Student Aid Recipients

Information on the individual characteristics of recipients is also useful for describing how student aid is distributed. Data from the 1986 NPSAS survey shows the percentage of all undergraduate students who received some form of federal aid by selected student characteristics. Overall, 35 percent of all undergraduates received aid. By race, 32 percent of white students, 33 percent of Asians, 41 percent of Hispanics, and 56 percent of Black students received some

form of federal assistance. Females were slightly more likely to receive aid than males; 36 percent of females received aid compared to 34 percent of males. Full time students were approximately three times more likely to receive federal assistance than part time students, according to the survey.

Nearly equal percentages of financially dependent versus independent students, 34 percent and 37 percent, respectively, were awarded federal aid in that year. However, this distribution varied by program. For example, while 18 percent of all students received a Pell Grant, only 14 percent of dependent undergraduates but more than 23 percent of financially independent students were Pell recipients. Conversely, while 20.5 percent of all undergraduates received a Stafford Student Loan, the dependent/independent split was a more uniform 21.1 versus 19.7 percent.

The increasing age of recipients is another indicator of the changing distribution of student aid. For instance, the percentage of Pell Grant recipients 22 years of age or younger has declined in the last decade, from 68 percent in 1978, to 64 percent in 1983, to 51 percent in 1986 (U.S. Department of Education, 1987). This mirrors general trends in higher education enrollments, where the percentage of students under the age of 25 has declined from 72 percent in 1970 to 62 percent in 1980 to 58 percent in 1985 (U.S. Department of Education, 1988).

The characteristics of vocational student recipients appear to be largely the same regardless of whether they are enrolled in proprietary or community college programs. For example, vocational students tend to

be from families with lower incomes than other post-secondary students, according to the 1986 NPSAS survey. Vocational students are also more inclined to be financially independent than other students -- roughly 53 percent of vocational students are independent, compared to 38 percent of all students. Evidence from other studies suggests that vocational students are more likely to be Black, female, and older than students in academic programs (Lee, 1987, and Wilms, Moore, and Bolus, 1987).

## II. Ways to Improve the Effectiveness of Student Aid

How have student aid programs performed relative to their central mission of supporting equality of educational opportunity? Much of the debate in this area has focused on both the capacity of the current student aid programs to fulfill this mission and their efficiency as vehicles for furthering the national goal of equal opportunity.

Despite the large infusion of funds into student assistance programs over the past several decades, participation rates in post-secondary education have not increased appreciably. Data from the Current Population Surveys (CPS) for 1970 to 1985, by family income group, show that participation rates for dependent students between the ages of 18 and 24 fell for all income groups in the first half of the 1970s, principally because of the end of the Vietnam War and the reduced pressure on males to enroll in college to avoid the draft. From the mid-1970s through 1980, participation continued to decrease for all but the very lowest income group. In the 1980s, however, the opposite trend has taken place: participation rates for the highest income groups have

increased moderately, while rates for the two lower income groups have remained constant or declined slightly (Hauptman and McLaughlin, 1988).

Concerns about participation are particularly acute for students from ethnic or racial minority groups. The percentage of black high school graduates aged 18 to 24 who completed at least one year of post-secondary education grew substantially between the early 1960s and 1975. Since 1975, however, participation rates have remained relatively steady for black students, reflecting a slight increase in participation for black females and a decrease in participation for black males. Participation rates for Hispanic students have also remained relatively constant, or modestly declined, during this period. Conversely, white student participation rates in college have edged upward slightly during the past decade.

These CPS data, however, only consider higher education enrollments, excluding most students in post-secondary vocational programs. To the extent that vocational programs enroll higher proportions of minority and disadvantaged youth, the trends in participation rates represent more of a transfer among post-secondary sectors than a loss in the overall number of minority students. Still, the apparent lack of progress in improving rates of participation for economically disadvantaged students, especially given the substantial amount of funds expended for student assistance annually, is troubling.

This section identifies ways in which the student aid system may have contributed to the lack of progress in improving the participation of low income and minority students in post-secondary education. These include the growing use of loans rather than grants as a primary means

for financial aid; the rapid increase in student loan default costs; the complexity in the delivery of student assistance; the inability to meet the needs of the rising number of older, nontraditional students; the extent to which the system no longer is targeted on those lower income college students for which it was primarily intended; and the marked decline over time in service-related benefits. Options suggesting ways in which these shortcomings might best be addressed are also included in this section.

### Redressing the Imbalance Between Grants and Loans

In the 1980s loans have become the primary form of student financial assistance. They now account for more than half of all student aid, a significant change from the beginning of the decade when they equaled 40 percent of all aid provided. It is even further from the mid-1970s, when loans represented less than 20 percent of the total aid provided and various types of grants represented close to 80 percent.

The shift from grants to loans can be attributed more to the growth of loans than to dramatic decreases in grant assistance. In real terms, loan volume has tripled from the early 1970s to the late 1980s. Grants did not increase as fast, particularly in the 1980s. With the rapidly rising cost of post-secondary education that has taken place since 1980, loans have filled the void and assumed a more prominent role in financing.

Eased eligibility requirements for the Stafford program in the late 1970s as a result of the Middle Income Student Assistance Act, and

more favorable terms for lenders, spurred the increased reliance on loans. The program grew from less than $2 billion in annual loan volume in 1977, to more than $6 billion in 1980, to nearly $12 billion in 1988, even though more restrictive borrowing requirements have been instituted in recent years. The entitlement nature of the program, and its off-budget financing that hides the "true" budgetary costs for many years after the loan is made, also helped to stimulate the growing emphasis placed on loans.

In a related way, the increasingly subsidized nature of the Stafford program over its two decade existence may also be a contributing factor. When it was created in the mid-1960s, the program was intended to provide essentially market-based loans of convenience to middle income students. Over time, however, the federal government has encouraged greater participation in the Stafford program by offering incentives to its various participants. Students benefit from below market interest rates and by having no repayment obligations until after graduation. Banks receive special allowance payments from the federal government that assure market rates of return -- regardless of the interest charged to borrowers -- plus a full federal guarantee in the event of default. State level guarantee agencies receive administrative cost allowances and federal reinsurance of all defaulted loans submitted for claims by banks, as well as collecting fees from borrowers.[8] The result is a program with attractive incentives for students to borrow and a powerful financial network with a considerable stake in encouraging students to borrow.

## Options for Redressing the Growing Grant/Loan Imbalance

One way of addressing the imbalance between grants and loans would be to strip away many of the subsidies that make the loans so attractive. This has already been done on a smaller scale in a subsidiary part of the Stafford program, the Supplemental Loans for Students (SLS) program. SLS relies on a variable interest rate, similar to market-based rates, and removes the costly in-school interest subsidies of regular Stafford loans; repayment begins 60 days after loan origination. Unfortunately, the existence of the more subsidized Stafford loans, combined with the fact that financially dependent students are not eligible to borrow in SLS, limits its potential impact. A reformed system in which less subsidized loans constituted a larger percentage of all loans might help to correct the grant/loan imbalance by making subsidized loans available only to those who truly need them.

To redress the imbalance between grants and loans, however, it is also important to increase funding for grants. The savings that could be achieved by restricting the availability of loan subsidies could be applied to higher funding levels for grant programs. Beyond this, greater resources for grants would help to stop the erosion in gains achieved by economically disadvantaged students in the early and middle 1970s.

## Reducing Student Loan Default Costs

One obvious and troubling consequence of the increased reliance on loans over the past decade is the growing cost of student loan defaults in the Stafford program. In fiscal 1987, federal default costs in the

Stafford program were $1.4 billion, representing more than 40 percent of total federal expenditures for the entire program. This is dramatically different from a decade ago, when federal default costs were just over $200 million and constituted less than 25 percent of program costs. The recent dramatic growth in borrowing under the SLS program -- where the majority of borrowers are from proprietary schools -- combined with projected increases in regular Stafford loan borrowing will likely push annual federal default costs over $2 billion in the next few years.

Most of the increase in default costs is a function of the larger number and amount of loans being made, rather than a marked change in the rate of default. For instance, loans in repayment have grown from $3.2 billion in 1979 to $23.6 billion in 1987, while the rate of default has not changed very much. U.S. Department of Education figures indicate that the default rate in 1980 was 12.5 percent, and in 1986 was 12.6 percent. However, the Department measures defaults on a cumulative basis. A better measure of changes in default activity would be an annual rate of default, a ratio of dollars defaulted in a given year to total dollars in repayment in that year. The annual default rate has hovered between 4 to 7 percent in the 1980s, measuring about 6 percent in 1987.

Vocational students have received a large amount of the attention in recent years because of their apparently higher incidence of default. Studies conducted in several states, including California, New Jersey, and Pennsylvania, show that community college students default more than twice as frequently as four year college students. Proprietary students default at an even higher rate, with annual default rates of 20 percent

or more in most cases. This has become an important issue for many schools because of recent Department of Education proposals to limit the participation in federal aid programs of institutions with high default rates.

Since the Carter administration, when student loan defaults were first raised as a serious public policy issue, periodic default reduction efforts have been made. These have included greater use of government and private collection agents and federal income tax refund offsets for student loan defaulters. While some gains have been made through these enhanced collection efforts, the best method for reducing defaults would be to prevent them before they occur. Prevention should, therefore, be a central part of any future plans for lowering default costs.

## Options for Reducing Default Costs

One way of reducing default costs would be to require more risk sharing amongst the major Stafford program participants. Currently lenders, guarantee agencies, and educational institutions assume little or no financial risk because of the 100 percent federal guarantee. As a result, few incentives exist to encourage program participants to keep defaults low. One means for sharing risks would be to require those lenders, guarantee agencies, and educational institutions with high rates of default to pay money into a loan insurance fund, which could then be used to offset the direct federal costs of default. It would also be helpful if the fees that borrowers currently pay were used to offset the federal costs of defaults.

Another avenue toward default reduction would be to provide "low income insurance" for those borrowers who have debt service obligations that exceed their ability to repay on a student loan. Many defaulters appear to be individuals who simply do not have enough income to meet their repayment obligations, and therefore default on the loan for lack of resources. Instead of being branded as "deadbeats," these borrowers should be able to appeal for help in meeting their obligations. Extended repayment terms, graduated payment schedules tied to income, and other alternatives could be devised to prevent these students from defaulting without increasing federal interest payments or other costs.

### Simplifying the Student Aid Delivery System

Another reason for the relative lack of effectiveness of student aid programs is how the aid is delivered to students. One of the most pressing problems of the current delivery system is its complexity, both for students and those who administer the program.

Students and their families are subject to a great many complexities in the student aid delivery system that may serve as a deterrent to their participation in higher education, especially among lower income students who may be intimidated by the process. Lengthy general application forms, such as the College Scholarship Service's Financial Aid Form, are much more complicated than the trimmed down 1040 tax forms that most lower and middle income families use. Other information, such as federal tax forms or supplemental application forms from institutions, is also frequently required for receipt of aid.

Further complications may arise when the aid is actually awarded to students, especially with student loans.

Many students also face an obstacle in the form of a general lack of information about the types and amounts of aid available, and incomplete information on the aid that has actually been awarded. Students and their families often fail to consider student assistance until well into the high school years, when poor family financial planning and the pressing problems of applications and other concerns may inhibit or discourage participation in post-secondary education. These factors may especially work against minority and low income students, who are often first generation college students and who would especially benefit from better and more complete early knowledge of student aid programs.

Institutional financial aid administrators have also seen exponential growth over the past two decades in the intricacy of student aid programs. In addition to the many institution-based and state aid programs, aid administrators have been hampered by complicated, time consuming, and often confusing rules about the administration of federal aid programs. Recent changes to program administration, including a federally mandated system of need analysis (formerly guided by an industry established standard known as the Uniform Methodology) and strict verification of student aid application data, have compounded the level of complexity.

**Options for Improving the Delivery of Student Aid**

The delivery system for student aid could be improved by simplifying the process of application, especially for the neediest students. Students with family incomes below the poverty level or some other minimum standard should be allowed to fill out a short, easy to comprehend form. This would ease application worries for those students who clearly should be receiving the most assistance, and may also help to reduce workloads for financial aid professionals. Simplification has been urged in many quarters for a number of years, but has consistently run into opposition from those who feel that the system should be designed to respond to small gradations in a family's economic circumstances. This simplicity/equity tradeoff is similar to that in the tax system, where arguments against simplifying the tax system have been fueled by fears that vertical and horizontal inequities would result.

More emphasis should also be placed on early awareness or early intervention programs. Programs that instill an understanding of the benefits of post-secondary training, as well as the availability of financial assistance, have multiplied in recent years. Eugene Lang's "I Have a Dream" Foundation, which guarantees access to higher education for "adopted" classes of inner city seventh grade students through financial assistance and counseling services, is considered the forerunner of many of these programs. This kind of assured access intervention appears to hold much promise based on the fact that virtually all of Lang's initial class of 60 students completed high school and over half have attended college. But it is too early to

evaluate most of the other "adopted" classes, and a "class-by-class" approach is too random to constitute a successful long-term public policy.

Efforts to institutionalize the Lang concept, such as New York State's recently adopted Liberty Scholarship and Partnership programs, also should be explored. The federal government could do its part in this area in one of several ways. It could provide more funds for the existing TRIO support services programs through which students receive tutorial, counseling, and other support through programs such as Upward Bound. It could also change the process for determining aid eligibility, moving up the time frame for analyzing need. For example, students in the seventh or ninth grade could be declared eligible for federal student aid on the basis of their family incomes at that time. This would ease concerns about being able to afford post-secondary education and might provide a greater incentive for academic achievement at any earlier age.

### Meeting the Financing Needs of Older, Nontraditional Students

Perhaps the greatest strain being placed on the student aid system at the present time is the growing number of older, nontraditional students. Most student aid programs have been designed to offer educational opportunities to young, full time students who are dependent on their parents for financial support. However, increasing numbers of older, often part time students are now enrolled in post-secondary education. Yet the student aid system's ability to meet the financial needs of these students has been marginal.

The trend toward older students has largely been fueled by demographic factors. The traditional college age cohort peaked in the early 1980s at approximately 30 million. Since then this age group has declined by nearly 15 percent, with expected declines through the mid-1990s of another 10 percent. While total higher education enrollments have remained steady in recent years, despite predictions to the contrary, the number of traditional college age students has declined. Current enrollment figures therefore reflect an increase in older students; more than 40 percent of all college students were age 25 and over in 1987, compared to just over 35 percent in 1980 and less than 30 percent in 1970.

The changing profile of students in recent years has also seen a shift toward more part time enrollments, which grew by nearly 90 percent between 1970 and 1985, while the number of full timers increased by only about 20 percent. Much of this increase in part time enrollments can be attributed to the growth in older students entering or returning to the world of post-secondary education.

The problems that these students present for the student aid system are many. Though the need-based financial aid system has tried to take the circumstances of nontraditional students into account -- by creating special rules for married students, those with dependents, and those who work fulltime and attend classes -- many needs remain unmet. Financial need, defined as the difference between student expenses and student resources, has become increasingly difficult to quantify rationally and equitably, particularly for the nontraditional student.

The central problem lies in the way student aid need analysis operates. Because student resources are largely a function of income in the year preceding the year of attendance, many older students, with higher incomes than recent high school graduates, do not qualify for assistance. But the higher cost of living expenses for older students, combined with support for dependents and other costs, are not fully taken into account, revealing a bias toward younger students that may discourage the participation of older individuals.

## Options for Meeting Nontraditional Student Needs

One way to improve the financing picture for nontraditional students would be to encourage the greater use of employer-paid education benefits. Unlike the traditional college age student, a principal form of assistance for older students is the tuition payments made on their behalf by employers. The benefits that employers and society in general receive from retrained and further educated employees are well documented. A sensible tax policy for employer-paid education benefits would serve to encourage the greater participation of members of the labor force in post-secondary education. Current law allows employers to deduct these expenditures as business expenses, while employees are not required to declare this assistance as taxable income. However, recent changes in the law have restricted this tax break to undergraduate expenses, a change which will limit the career enhancement potential of employer financed benefits. It has also renewed pessimism about the long-term viability of this tax benefit. A sound policy might

be to restore fully the tax exemption for all employer-paid post-secondary expenses and to make it a permanent section of the tax code.

Another important avenue for enhancing the educational opportunities of the workforce involves the retraining of unemployed and dislocated workers. Very little student financial aid is currently provided to individuals who are unemployed, particularly those who are seriously dislocated through plant closings or other local economic downturns. What little is provided is not available in a systematic way that allows displaced workers to make the transition between jobs and careers. The Department of Education student aid programs, as has already been mentioned, are not constructed with the older students in mind. A handful of colleges and universities provide reduced or zero tuitions for dislocated workers and farmers, but this hardly represents a concerted effort. Department of Labor programs through the Job Training Partnership Act do provide stipends for unemployed and dislocated workers. But these DOL provisions are generally underfunded relative to need, cannot be used for tuition expenses, and they are largely limited to vocational programs.

What is needed is a partnership of the federal and state governments, colleges and universities, trade schools, and the private sector that would provide adequate financial aid to dislocated workers to help meet their education and retraining needs in a broad range of areas. The federal government and the states should be willing to make stipend payments that help cover the living costs of the workers and their families while they are undergoing retraining. Colleges and universities, as their contribution to the partnership, should be

prepared to reduce substantially or totally waive their tuitions for these students. If the partnership is to succeed, companies and unions must also participate by contributing funds for these purposes.

### Targeting Student Aid on Intended Beneficiaries

As the federal approach to student aid was being developed in the late 1950s, one of the central goals was to encourage more participation in higher education programs in the sciences, engineering, and other areas of national interest. The concept of equal educational opportunity introduced in the 1960s broadened this strategy to include opening opportunities for students from lower socioeconomic backgrounds to pursue a post-secondary education. The result was a significant increase in the number of students participating, especially through the mid-1970s.

Over time, however, the focus of the student aid programs on increasing the college participation of economically disadvantaged students has been diluted in two principal ways. One change began in the early 1970s with the inclusion of proprietary school students in the definition of eligible student aid recipients. Because of this change, the term "post-secondary education" was introduced to make note of this broader eligibility. A consequence of this changed definition of who should receive federal student aid dollars is that students pursuing distinctly different forms of education now compete for the same dollars. The higher proportion of low income students who attend proprietary school programs has led to increased student aid funds going to students in this sector. Given the constraints on federal funds, the

diversion of federal dollars to proprietary school students has led to a serious erosion in the amount of aid being delivered to students in traditional higher education programs.

In the past decade, the number of collegiate students who receive federal aid has declined substantially. For example, Pell Grant recipients in proprietary schools grew from 286 thousand in 1980 to 633 thousand in 1986, an increase of 120 percent, while the number of collegiate Pell recipients declined, from 2.42 million in 1980 to 2.03 million in 1986, a decrease of over 15 percent (U.S. Department of Education, 1987).

The other change in student aid eligibility that may have contributed to decreasing program effectiveness is the growth in the number of middle income students who receive aid. Federal student aid's ability to serve adequately the needs of disadvantaged students has been hampered in recent years by legislative changes that would extend aid to higher income students. Because of limited program funding, these changes have resulted in enhanced eligibility for higher income students at the expense of lower income students for whom most aid programs have been designed.

One example of these changes is in the Pell Grants program, where the eligibility formula has changed significantly since the program was established in 1973, resulting in increasing numbers of awards to students who initially would have been ineligible. Examples of more favorable treatment for middle income students include more lenient rules for families with more than one child in college at the same time, and an allowance for state and local taxes. The proportion of Pell aid

going to middle income students, as a result, has increased somewhat over time. It would have increased even more except that limits in the overall funding for Pell Grants act as a constraint on the growth in income eligibility for the program (Mortenson, 1988).

It also appears that "middle class creep" has occurred in the way that institutions provide aid from their own resources. As the number of traditional college age students has declined, many institutions have competed for this declining pool of students has been to provide more aid on the basis of merit or simply to give more aid to middle income students as a way of encouraging them to attend a particular institution. This competition for students through aid represents a serious erosion in the need-based student aid system as it has operated over the past 35 years.

## Options for Targeting Aid on Intended Beneficiaries

In a world of unlimited resources, extending student aid to students in proprietary schools and those from middle income families would be a good policy to follow. But in the real world of limited resources for student aid, expanding aid to some groups of students serves to limit severely the impact of student aid dollars on their primary beneficiaries. To improve the effectiveness of student aid programs in helping economically disadvantaged students go to college, therefore, it may be necessary to target the resources more than is currently the case.

One way to target funds would be to place some restrictions on the amount of aid provided to proprietary school students for student aid.

This might be done, for example, by setting out different award and loan schedules for students in collegiate and vocational programs. While this could be interpreted as discrimination, there is considerable precedent in the student aid programs, particularly loans, where the amount of aid provided varies with the level of education. In the current Stafford loan program, first and second year students can borrow a maximum of $2,625, while third and fourth year students can borrow up to $5,000, and graduate and professional school students can borrow up to $7,500 annually.

Another avenue to pursue is to limit the eligibility of students who do not have a high school degree or equivalent but nonetheless qualify for aid under the "ability to benefit" provisions in the legislation. If an institution determines that a student without a high school degree could benefit from post-secondary training, then the student is deemed eligible for aid. This provision, which essentially only applies to students in vocational programs in proprietary schools or community colleges, is one of the greatest abuses of the current system because institutions do not take sufficient care in determining which students indeed have the ability to benefit. At a minimum, it would seem appropriate to end the eligibility of these students to borrow. Under the current arrangement, students without a high school degree are allowed to borrow fairly large sums of money for a very unpredictable benefit.

A further step in this direction would be to remove students without a high school degree from the post-secondary student aid programs and place them instead in the vocational training programs of

the Department of Education and the Department of Labor. Another possibility would be to shift the eligibility of all post-secondary vocational students into other programs, either into existing Department of Education and Labor programs or into a new, separate program of post-secondary vocational aid. Such a change would certainly represent a shift from the federal policy established in 1972 with regard to vocational programs, and many would oppose it for this reason. But no one at that time imagined the large shift in the distribution of resources that would occur, or the degree to which such a shift might limit the aid provided to disadvantaged students who want to go to college, which was the initial focus of the legislation.

With regards to the shift in student aid funds toward middle income students, the obvious way to target funds is to change program formulae to restrict the eligibility of these students for aid. For example, it may no longer make sense simply to divide a family's contribution by the number of children in college -- this is the provision that now allows students from families with incomes in excess of $100,000 to receive subsidized loans. It might be more appropriate to return to the initial formulation in the Pell Grant program and the need analysis systems where families with two children in college were expected to contribute more than a family with one child in college, but not twice as much. Other changes that have been enacted, such as making allowances for state and local taxes in calculating family contributions, should also be reviewed on equity grounds.

## Linking Student Aid with the Performance of Service

Providing aid in return for service represents one of the oldest forms of government student assistance. In the 1930s, the federal government provided small matching grants that encouraged states to establish work-study programs for Depression-era students. The GI Bill, the largest of the student aid programs, was clearly service-related. The College Work Study program, established in 1965, provides an opportunity for college students to work while in school as a means of paying a portion of their costs of attendance. Another form of service-related aid was also enacted in 1965 when the Social Security program was expanded to provide benefits for the post-secondary educational costs of the 18 to 22 year old children of program beneficiaries.

In the three decades following the Second World, service-related aid grew to be the largest form of student aid; in 1975, it accounted for over half of all student aid provided. Since the mid-1970s, however, service-related aid has dramatically decreased as a proportion of all student aid provided. Veterans educational benefits have declined and Social Security educational benefits have been phased out entirely. Funding for College Work Study program has been relatively level since 1980, meaning that the real value of such assistance has dropped by about a third in the 1980s. For all three service-related programs combined, funding has dropped by 85 percent in real terms since the mid 1970s, and it now accounts for less than 10 percent of all aid provided.

In recent years, a growing number of proposals have been made to renew the linkage between the performance of service and the receipt of

student aid. The motivations for these proposals vary widely. Some aim to rekindle a sense of voluntary spirit among American youth. Others are designed to provide an alternative to the military draft. Still others seek to develop a greater commitment to service over a lifetime. The variety of national service programs that have been proposed in recent years reflect this diversity of objectives.

At least one of the national service proposals also emanates from a sense that the current student aid programs are not working as well as they should and that having students perform service in return for aid would improve the effectiveness of -- and the political support for -- the concept of student aid. This formulation of national service was first proposed by the Democratic Leadership Council and is embodied in legislation introduced by Senator Sam Nunn and Rep. Dave McCurdy. Under the proposal, high school graduates could serve for one or two years in a Citizens Corps in tasks such as assisting in hospitals, serving as tutors in schools, or helping in environmental projects. In return for this service, members of the Corps would receive a modest stipend and the payment of a benefit that could be used either to help defray their post-secondary educational costs or as a downpayment for a home. It is fair to say that this proposal has moved the idea of national service to the forefront of national issues.

The most controversial aspect of the Citizens Corps concept is the proposed requirement that most students would have to perform service in order to be eligible for federal student aid. Critics point out that this service requirement would create a two-tiered system in which students from middle and upper income families would be able to attend

based on their parents' financial resources, but those from economically disadvantaged circumstances would be forced to serve in order to go to college. The Citizens Corps approach could be very expensive in that it would provide benefits that are at least several times larger than what students currently receive in the student aid programs. If the same number of students were to receive aid under the Citizens Corps approach as now receive student aid, the program would cost tens of billions of dollars.

## Options for Encouraging Service Through Student Aid

One option for encouraging service is to adopt the Citizens Corps approach as proposed. But the controversy surrounding its service requirement represents a substantial obstacle to its legislative adoption. In addition, the Citizens Corps would only be for recent high school graduates. This restriction means that individuals without high school degrees or their equivalent, the "forgotten half" of Americans who do not go on to college, would be ineligible for either educational or housing benefits under the current proposal. As a result of this restriction, students in vocational programs would not be able to participate fully.

One modification to the Citizens Corps concept that would greatly enhance its political viability and its fairness would be to drop the service requirement. Under such a situation, students who performed service would receive larger benefits than what non-servers receive through the existing set of student aid programs. This arrangement would be analogous to what happened with the GI Bill in the late 1960s,

1970s, and 1980s when it has coexisted with the student aid programs. Another possible modification to the Citizens Corps proposal is to maintain the current availability of grant assistance for lower income students, but to allow students from all income levels to choose between service and loans. That is, a student could borrow to pay for the costs not met through family resources and grant assistance, or could opt for service to make up the difference between costs and family/grant assistance. The Citizens Corps would also be fairer if non-high school graduates were eligible for educational and housing benefits.

Another approach is to set up a system in which benefits are provided for service that is performed at different times of the lifecycle. For example, a modified Citizens Corps for recent high school graduates as described above might reasonably be combined with enhanced work-study benefits for community service performed by college students and with loan forgiveness for college graduates who choose to enter designated public service professions such as teaching or nursing. Service over a lifetime might also be encouraged through an arrangement similar to the National Guard in which individuals who served in their communities on weekends in return would receive educational or housing benefits, such as has been proposed by Senator Barbara Mikulski. Stipends or benefits might also be provided to retired individuals who participated, a provision which is included in the Citizens Corps proposal.

Given the uncertainties surrounding the national service concept at this time, however, it does not make sense to implement a full scale program. Instead, whatever program is enacted should be initially

conducted through demonstration projects as a way of testing the various avenues for expanding national and community service opportunities.

## NOTES

[1] The terms "higher education" and "collegiate education" encompass students in four and two year public and private institutions, including community college vocational students, but exclude all students in proprietary institutions. "Post-secondary education" refers to all forms of education and training beyond the high school level.

[2] Data for student aid are sometimes adjusted significantly over the course of several years. As a result, considerable faith should not be placed in data suggesting a sharp increase in aid in 1987 until more accurate and complete information is available.

[3] Other sources of student assistance also exist, though reliable data overtime are not available for all such sources. Estimates of two of the most important sources, employer-paid assistance and state-level loan programs, suggest that, combined, approximately $2 billion annually is provided to students pursuing post-secondary educations (Hauptman, 1989, and Merisotis, 1988). Therefore, a reasonable approximation of total student aid in recent years would be in the $25 to $27 billion range. Excluded from this total would be any aid provided from other private or philanthropic sources, for which no reliable estimates exist.

[4] In this paper, student assistance programs are divided into three broad categories. Grants and Fellowships includes all grant assistance that is awarded based on need. This includes three federal programs,

Pell Grants, Supplemental Educational Opportunity Grants (SEOG), State Student Incentive Grants (SSIG), as well as state grant programs and institutionally awarded grants. Service-Related Aid is grant and work assistance that is targeted to specific beneficiaries in return for some type of service. This includes Social Security benefits, Veterans Education benefits, military benefits, the federal College Work Study (CWS) program, and other, comparatively small federal grant programs for students in health professional, legal, and other fields of study. Student Loans comprise the Stafford Student Loan (formerly Guaranteed Student Loan) program, the Perkins Loan (formerly National Direct Student Loan) program, and other, small federal loan programs for students in various health-oriented fields of study.

[5] The campus-based programs are administered directly by financial aid administrators at participating schools. The application for, and awarding of, aid through these programs is determined by the institutions in accordance with federal guidelines.

[6] More complete data on the extent of borrowing in the Stafford program, by sector, may be available in late 1989 because of new federal data reporting requirements.

[7] It has been estimated that roughly half of all community college students, on a full time equivalent basis, are entered in terminal vocational programs (Lee, 1987). Since the receipt of need-based aid is not conditioned on the type of program or field of study, it is

therefore reasonable to assume that roughly half of all student aid awarded to community college enrollees is received by students in vocational programs.

[8] A guarantee agency will receive less than 100 percent reinsurance if its annual default rate (defined slightly differently than prescribed here) falls below certain levels.

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